

Five Year Review

All figures are expressed in thousands unless otherwise specified.

	1986	1985	1984	1983	1982
Production—KCl Tonnes					
Allan Division	517	388	569	373	478
Cory Division	772	563	743	599	542
Esterhazy Division	669	774	965	718	715
Rocanville Division	1,478	903	1,358	887	822
Lanigan Division	165	618	867	529	309
Total PCS Mining	3,601	3,246	4,502	3,106	2,866
Total Canadian Producers	11,040*	10,882*	12,703*	9,719*	8,538
Sales—KCl Tonnes					
North America	2,062	2,073	2,204	2,193	1,481
Offshore	1,703	1,291	1,849	1,399	1,168
Total PCS Sales	3,765	3,364	4,053	3,592	2,649
Total Canadian Producers	11,343*	10,630*	11,494*	10,795*	8,256
*includes producers in New Brunswick					
Financial (\$)					
Gross Revenue	155,327	197,311	277,797	217,702	192,127
Income before Taxes and Interest	(47,007)	(6,880)	65,044	9,116	21,701
Provincial Taxes	13,309	10,773	17,692	10,822	15,020
Interest Expense	43,084	31,986	22,003	16,301	6,074
Net Income (Loss) before extraordinary items	(103,400)	(49,639)	25,349	(18,007)	607
Dividends declared	—	—	12,000	62,000	50,000
Gross Payroll & Benefits	58,367	60,668	67,071	59,780	64,660
Capital Expenditures including capitalized interest (net)	59,719	95,375	113,931	111,638	140,454
Cash Flow from Operations	(12,912)	20,048	57,160	99,910	13,926
Working Capital	(29,250)	(107,274)	33,868	(41,248)	(26,854)
Long Term Obligations	662,414	446,970	455,464	372,980	221,787
Shareholder's Equity	505,889	609,289	678,022	602,673	682,680
Return on Equity—Pretax	(16.16%)	(6.04%)	6.72%	(0.08%)	2.21%
—After tax	(18.54%)	(7.71%)	3.96%	(2.80%)	0.09%
Employees at year end (actual numbers)	1,668	1,756	1,917	1,826	2,191
1986 Quarterly Results		Q1	Q2	Q3	Q4
Sales—KCl Tonnes		956	1,029	891	889
Production—KCl Tonnes		1,023	863	762	953
Gross Revenue		24,895	57,580	33,408	39,444
Net Income (Loss) before extraordinary item		(36,111)	(9,190)	(30,245)	(27,854)
Cash Flow from Operations		(40,560)	48,811	10,006	(31,169)

Letter of Transmittal

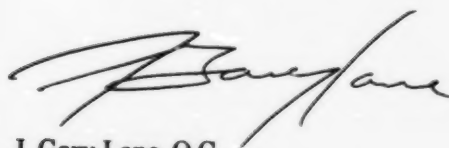
March, 1987

To His Honour,
The Honourable Frederick W. Johnson
Lieutenant Governor of the
Province of Saskatchewan

Sir:

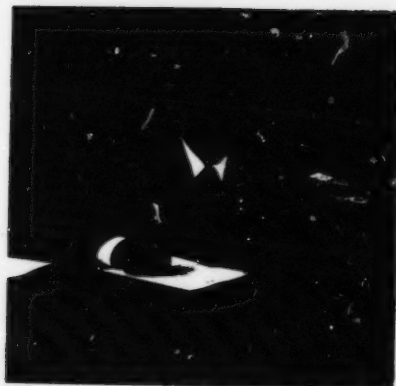
I have the honour to submit the Annual Report of the Potash Corporation of Saskatchewan for the year ended December 31, 1986, including the financial statements in the form required by the Treasury Board and duly certified in accordance with The Potash Corporation of Saskatchewan Act.

I have the honour to be, Sir,
Your obedient servant

A handwritten signature in dark ink, appearing to read "J. Gary Lane". The signature is fluid and cursive, with the first name "J." and last name "Lane" clearly distinguishable.

J. Gary Lane, Q.C.
Minister-in-Charge of the
Potash Corporation of Saskatchewan

Chairman's Message



Mr. Cliff Wright, Chairman

... was the tenth year of operation for the Potash Corporation of Saskatchewan and its subsidiaries, PCS Mining and PCS Sales.

The first five years marked the Corporation's entry into the market place, a market place which foresaw the long term outlook as bright for the potash industry with potash demand remaining relatively high to production until the middle of the '80's. The Corporation thus embarked on major expansions which would come on stream and make further supplies available to meet the predicted heavy demand situation.

Unfortunately the predictions did not come to pass. The world economic recession heavily impacted on the demand for potash in our market places and on the economic livelihood of our customers. As well, major expansions of mining facilities to meet the predicted heavy market demand had begun which had long term financial obligations for PCS.

Thus the past five years have damaged the financial viability of the Corporation. In 1986, we experienced the least favourable financial record in our ten year history. For the year ended at December 31, 1986 losses totalled \$103,400,000.

Although many factors have contributed to this financial loss we are, along with other producers in the industry, experiencing economic factors which have impacted directly on the Corporation. Most notably, 1986 saw a substantial drop in the price of potash in our domestic market; and a severe drop in the product's demand primarily in the heavy use areas of North America.

While the Corporation has experienced hard times it continues to be among the industry leaders in mine operations and technology, transportation, customer service and research and development.

In 1986 PCS Sales' domestic sales were close to 2.1 million tonnes, fractionally below 1985 sales. PCS Mining produced 3.6 million tonnes despite a major strike at its Lanigan mine site.

Together the two subsidiaries combined efforts to improve transportation via truck deliveries from PCS Mining, Rocanville Division. Upgraded highway accesses to the mine site will permit year-round growth in truck movement of the product to customers.

The Board of Directors met eight times during 1986. Mr. Cliff Wright served as Chairman of the Board from November 10, 1983 to December 31, 1986 and the Board and Corporation express their sincere thanks to him for his leadership and service.



As the Corporation moved into its second decade it became necessary to streamline efficiencies and downsize the Corporation's structure. This led to significant changes to the Corporation in March 1987. These changes reflect the overall need to turn the Corporation around and head it towards a successful and profitable future. The challenge facing us is immense but it is by striving to meet such challenges that people pull together and thus attain corporate and individual goals.

It is our hope that during 1987 the Corporation along with its employees will continue to meet the challenges and move on to build a stronger and more productive company.

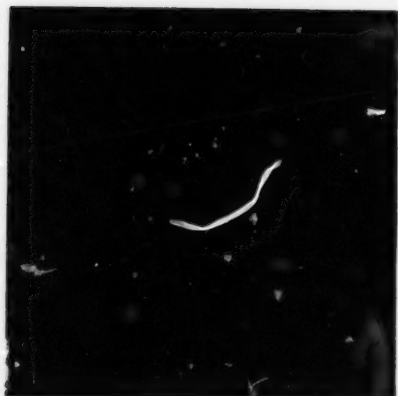
Paul Schoenhals

P. J. SCHOENHALS
Chairman of the Board

Above: Self-unloading Great Lakes carrier discharging potash at Port Stanley, Ontario.

Left: PCS Sales has a fleet of approximately 1,000 rail cars.

PCS Mining



roduction from our mining operations was 3.6 million tonnes of KCl during 1986, an increase of 0.4 million tonnes over 1985.

The collective bargaining agreements at all Divisions expired during 1985. A new agreement was reached with Rocanville Potash Employees' Association, with expiry in 1989. Negotiations for new agreements at Allan, Cory and Lanigan were imminent but not concluded at year end. At Lanigan Division, a strike commenced March 10, 1986 and continued through year end.

Employment within PCS Mining was 1,538 persons at December 31, 1986, down 73 from 1985. This change resulted from resignations at the Divisions and a 27 percent reduction at the Saskatoon office.

During 1986, PCS Mining did not carry insurance on the underground portion of its mining properties.

Allan Division

Production at the Allan Division was 0.861 million tonnes, up from 0.712 million tonnes in 1985. Operations were on a three shift basis with 400 people. PCS Mining's 60 percent share was 0.517 million tonnes. The remainder is owned by our co-tenant, Saskterra Fertilizers Ltd., who acquired the holding of Kidd Creek Mines Ltd.

Allan Division was the winner of the Saskatchewan Mine Rescue Competition and represented the province at the National Competition held in Nanaimo, British Columbia.

Cory Division

At PCS Mining, Cory Division, 1986 production was 0.772 million tonnes. This compares to 0.563 million tonnes produced in 1985.

Productivity improvements of 24 percent over 1985 were realized mainly as a result of the revised mining plan incorporated in late 1985.

Modifications to the mill enabled the Division to produce a Granular product with a high market acceptability. As well, the first commercial sales of Sulphate of Potash were made. Production from this unit improved steadily throughout the year.

The Division operated on a three shift basis with 319 employees.

Esterhazy Division

Product is mined and refined from ore reserves owned by PCS Mining at Esterhazy and produced under a long term processing agreement with International Minerals and Chemical Corporation (Canada) Limited.

Production was 0.669 million tonnes compared to 0.774 million tonnes in 1985.

A major brine inflow at the beginning of the year in IMC's K-2 mine caused a slowing of production. Significant expenditures were necessary to control the inflow.

Three PCS Mining employees handle the loading and shipping co-ordination at this Division.

Lanigan Division

The Division's total production for 1986, on a three shift operation, was 0.165 million tonnes compared with 0.618 million tonnes in 1985.

On March 10 all unionized employees, members of the Energy and Chemical Workers' Union, withdrew their services. This strike remained unresolved at year end, although talks between the parties had resumed.

Supervisors manned the operations during the strike, continuing work on all major underground and surface projects, completing outstanding maintenance work and operating the production facilities during the late spring.

Completion of the Phase II Expansion project was curtailed in August awaiting the resolution of the strike.

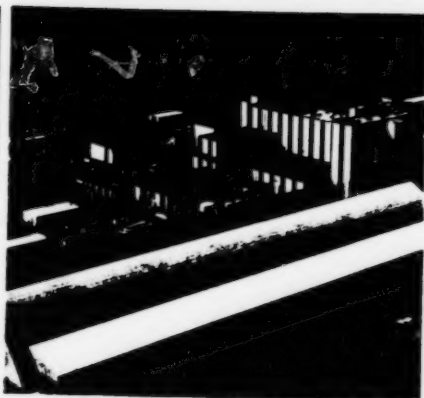
Employment at Lanigan was 305 production personnel and 33 Phase II Expansion personnel.

Rocanville Division

During 1986 a yearly production record of 1.478 million tonnes was achieved, surpassing the previous high of 1.358 million tonnes in 1984 and compared to 0.903 million tonnes in 1985, when production was curtailed due to the inflow of brine.

The Division continued on a four shift operation and employed 393 persons.

The underground concrete plug, which stopped the major brine inflow in 1985, was resealed in April and appears to be stable. Condition of the plug is monitored by instrumentation and by regular personnel checks.



PCS Mining, Rocanville Division



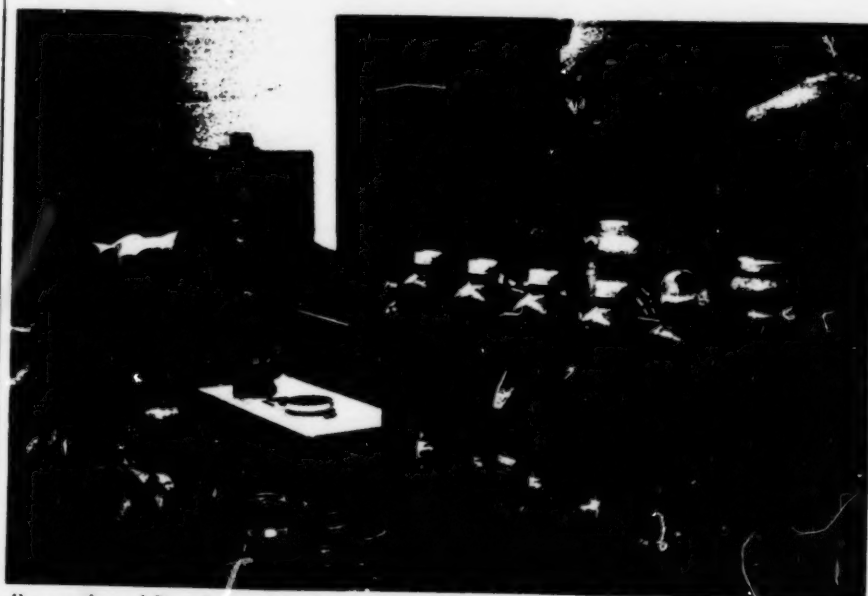
PCS Mining, Lanigan Division



PCS Mining, Cory Division



PCS Mining, Allan Division



Research and Development

PCS Mining entered into an agreement with the Saskatchewan Department of Highways and Transportation to upgrade the industrial access road from the main highway to the Rocanville plant. This allows our customers to haul primary highway weight loads from the operation year round. An increase in truck movement was noted in 1986 when 7,025 trucks were loaded.

Research and Development

Various Research and Development projects were directed at technologies to achieve greater production efficiency, increased recovery of potash, enhanced safety, high quality, reduced cost and new potash products.

A prototype ore grade analyzer was commissioned on a mining machine and an automated advance unit was installed for trials.

Patents were received for the Integrated Acoustics Network. This system is utilized to locate and warn of micro-seismic events and potential rock falls.

Advance identification of anomalies, especially water bearing, was investigated through longhole drilling, geotomography, pulse electromagnetics, radar and other methods.

A prototype automatic particle size analyzer was completed and readied for field trials.

PCS Sales

Potash markets in 1986 reflected the world over-supply with sales volume and revenues remaining below desirable levels.

Preliminary indications are that world potash demand was off in 1986, primarily in the heavy use areas of North America and western Europe.

Deliveries from Canadian and U.S. producers to North American destinations were 7.8 percent below 1985 levels. The PCS Sales volume remained relatively stable, being off only marginally.

The offshore markets, in which Canada participates, recovered primarily due to sales in Brazil and China. Canpotex, the Saskatchewan producers' export marketing company, registered sales of 3.5 million tonnes, an increase of 21 percent. The PCS Sales share in Canpotex was 1.7 million tonnes, or 49 percent.

The outlook for potash markets in 1987 remains clouded by large excess in installed capacity, and an expected continuing drop in demand in North America and western Europe as a result of the depressed agricultural situation. It is expected that offshore markets will show a modest improvement over 1986 levels. Some uncertainties have arisen relative to supply but these are not expected to sufficiently compensate through improvement in revenues for the shrinking North American volume.

North American Agriculture

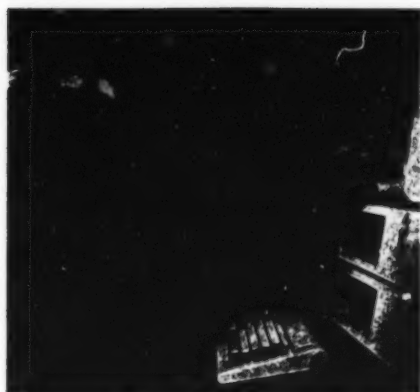
Unprecedented changes are impacting every phase of agri-business creating significant structural adjustments within the system and among the relationships of producers-suppliers, dealers-retailers, farmers-consumers, and the government.

Farms are getting larger, becoming more specialized, yet remain vulnerable to market fluctuations, internal operating problems, and financial pressures.

Management emphasis is on efficiency. The need for greater price-orientation has changed traditional relationships. Cash flow is often the deciding factor in a farmer's decisions, rather than level of profitability.

At the same time, we are seeing small farmers who derive a major portion of their income from off-farm sources in those geographic areas which provide off-farm employment opportunities. This is an important development; this group of farmers is less vulnerable to market swings, has different needs, and is less price-sensitive in its buying negotiations.

In the U.S. it is projected that within the next five years some 50,000 farmers will produce some 75 percent of farm products. These farmers will be served by a new dealer-retailer who requires different services from his suppliers than exist today.



PCS Sales supplies North American dealers with support services for farmer customers



Potash is an essential plant nutrient for crop production.



PCS Sales potash warehousing system provides same day delivery across North America.

In North America, approximately 20-30 percent of farmers are facing serious financial problems; 70-80 percent are in reasonable or good financial condition but are nervous and cautious. It is unfortunate that many young progressive farmers who purchased land a few years ago at high prices are unable to make ends meet and have become very disillusioned. In many instances, it will require selling their land to investors to enable these farmers to continue.

The North American fertilizer industry faces painful adjustments to the paradox and dilemma of the global agricultural situation. Important markets for major crops have been lost, commodity prices have plunged, farm equity values have dropped. In the U.S. grain exports have declined sharply, government payments have skyrocketed, and the farm credit system is in trouble. Surplus inventories continue to lower farm gate prices. The U.S. government encourages acreage set-asides. All this has resulted in less demand and lower prices for farm inputs, including fertilizers.

The situation will remain difficult for some time. The agricultural dilemma is global in origin and impact as surpluses are an international problem. The resolution of the crisis may at some point well depend on a multi-national willingness to overcome domestic political concerns and a move towards rationalization of production on the basis of comparative advantage and free trade.

North American Markets

In the fertilizer industry there has been consolidation of the dealer-retailer segment since the large grain companies began acquiring retail fertilizer businesses. Large fertilizer manufacturing companies continue to withdraw from agri-business. The Cooperatives are changing priorities and objectives from supply-orientation to a profit-oriented customer-driven marketing approach.

These events have had a direct and serious impact on potash sales. In the 1975-81 period when planted acres, prices and agricultural land values were rising, potash consumption in the U.S. grew at 6.3 percent per year on average and potash application on a major crop such as corn grew at average 4.8 percent per year. In the 1982-85 period, planted acres, prices and land values fell; potash consumption dropped 2.5 percent per year on average along with potash application on corn at 2.0 percent.

Potash sales in North America have fallen by more than 3 million tonnes product from their peak of over 11 million tonnes in 1979. In 1986, sales by North American producers were 8.8 million tonnes KCl, 7.8 percent below 1985. PCS Sales domestic sales were close to 2.1 million tonnes, fractionally below the 1985 tonnage.

The dealer-retailer cannot expect much relief in 1987 from the problems of the early 1980s. The trend of the last few years, which has disastrous impact on producers, will affect the dealer-retailer in the near future. There will be a reduction of the number of dealer-retailers as the problems with farmers continue to plague the industry. The number of distributors will likely be 50 percent of the current level by 1990. The structural change at the dealer level will impact PCS Sales' marketing strategies as the dealer's own customer base is undergoing change.

The outlook for 1987 and beyond is dependent on the resolution of the agricultural dilemma. The growth in food production in developing countries clearly limits traditional exporters of agricultural goods such as Canada and the U.S. in their efforts to rebuild export sales rapidly. The rising cost and questionable consequences of the U.S. farm support programs open the possibility of "decoupling" farm income support from crop production.

It is expected that potash shipments in 1987 in North America will fall another 5-6 percent.



*Lange-Stegmann Fertilizer Company,
St. Louis, Missouri.*



Potash application on oil palm plants in Malaysia.

Offshore Market

Canpotex, the Saskatchewan producers' offshore marketing company sold 3.5 million tonnes in 1986 representing an increase of 21 percent. This level of sales was exceeded previously by the record 4.2 million tonnes achieved in 1984. Canpotex strengthened its position in the key Brazilian market and participated in the resumption of sales to China, while maintaining traditional levels in other markets.

During the year Canpotex introduced new logistical approaches to offshore markets: a rail-barge system via the New Orleans gateway for Central and South America and a combined rail-vessel system via Thunder Bay to Europe.

The worldwide surplus manifested itself in a sharp reduction in revenues as prices continued to fall throughout the year.

PCS Sales supplies 49 percent of potash sold by Canpotex, increasing sales to 1.7 million tonnes from 1.3 million in 1985.

For 1987, it is generally expected that demand in offshore markets could show modest improvement, except for China where it is anticipated that a new record in purchases may be set. We need to recognize that demand in China is trending upwards but will likely continue to fluctuate significantly from year to year. Export revenues will remain under pressure although moderate recovery from today's level may be achievable.

Operations

At year end, there were 84 employees in PCS Sales, of whom 60 were located at the corporate Head Office in Saskatoon. Twenty-four employees in the Chicago-based U.S. sales group provide close customer contact and marketing support in major consuming areas.

Within North America, PCS Sales' warehouse system remains an essential element in our marketing strategy. Two wholly-owned warehouses at Fort Dodge, Iowa and Burns Harbor, Indiana are staffed by PCS Sales employees. The ability to provide easy and prompt access to potash during peak demand period was demonstrated in April when record sales volumes were achieved. The rail and water transportation systems which complement in-market warehouses remain the work-horse of our transportation system. In a competitive market, it is essential to tailor these bulk distribution systems to individual customer needs. With the cooperation of Canadian and U.S. rail and water carriers, the distribution system is constantly adjusted to the requirements of the market.

Truck deliveries from PCS Mining Rocanville Division increased sharply. Upgraded highway access permitting year-round primary highway weights is expected to result in sustained growth in truck movements.

The warehouses owned in the Port of Vancouver are assigned to and operated by Canpotex Limited in support of offshore sales.

The importance of an agronomic support system was demonstrated in China. The Potash & Phosphate Institute of Canada, in conjunction with Canpotex Limited, undertook major demonstration and promotion activities which include the support of the Canadian and Saskatchewan governments. These activities have contributed to increased awareness among Chinese farmers of the need for balanced fertilization and to accelerate demand for potash overseas.

The increased offshore market development programs parallel the success of the Potash & Phosphate Institute in North America. PPI programs emphasize maximum economic yields as a means for farmers to survive in economically difficult times. The PCS Sales Agronomy Department has complemented these programs through inhouse publications and services as well as support for independent research.

Auditors' Report

To the Members of the
Legislative Assembly of
the Province of Saskatchewan

We have examined the consolidated statement of financial position of Potash Corporation of Saskatchewan as at December 31, 1986 and the consolidated statements of income and retained earnings and of changes in cash flow for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at December 31, 1986 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceeding year.

January 31, 1987
February 10, 1987 as to Note 16
Saskatoon, Saskatchewan

Alberto Hadwin & Sons
Chartered Accountants

**Consolidated Statement
of Financial Position**

As at December 31

	(Thousands)	
	1986	1985
Assets		
Current Assets		
Accounts receivable	\$ 51,025	\$ 67,844
Inventories (Note 4)	47,043	51,950
Deposits and prepayments	20,249	20,121
	118,317	139,915
Fixed Assets (Note 5)	1,164,744	1,130,684
Deferred charges and investment (Note 6)	32,809	32,849
	\$ 1,315,870	\$ 1,303,448
Liabilities		
Current Liabilities		
Short-term debt		
Banks	\$ 24,721	\$ 110,145
Province of Saskatchewan	50,000	50,000
Accounts payable and accrued charges	63,289	65,750
Current portion of long-term debt	5,690	5,699
Current obligations under capital leases	3,867	3,595
Dividend payable	—	12,000
	147,567	247,189
Long-term debt (Note 7)	558,206	339,205
Obligations under capital leases (Note 8)	104,208	107,765
	809,981	694,159
Contingency (Note 16)		
Equity		
Province of Saskatchewan investment (Note 9)	480,554	480,554
Retained earnings	25,335	128,735
	505,889	609,289
	\$ 1,315,870	\$ 1,303,448

**Consolidated Statement
of Income and
Retained Earnings**

**For the Years
Ended December 31**

	(Thousands)	
	1986	1985
Income (loss)		
Sales	\$ 189,657	\$ 195,781
Foreign exchange	(38,068)	(4,108)
Interest and other	3,738	5,638
	155,327	197,311
Costs and expenses		
Operating costs other than those shown below	133,779	135,091
Depreciation and amortization	33,970	32,713
Research and development	3,458	4,698
Selling, distribution and administrative	31,127	31,689
	202,334	204,191
Operating Loss	(47,007)	(6,880)
Interest expense (Note 10)	43,084	31,986
Loss before taxes and extraordinary item	(90,091)	(38,866)
Provincial mining taxes (Note 11)	13,309	10,773
Loss before extraordinary item	(103,400)	(49,639)
Extraordinary item	—	(19,094)
Net Loss	(103,400)	(68,733)
Retained earnings—beginning of year	128,735	197,468
Retained earnings—end of year	\$ 25,335	\$ 128,735

**Consolidated Cash
Flow Statement**

**For the Years
Ended December 31**

	(Thousands)	
	1986	1985
Operating Activities		
Operating loss	\$ (47,007)	\$ (6,880)
Provincial mining taxes	(13,309)	(10,773)
Non-cash items—depreciation and amortization	28,267	30,438
Decrease in non-cash working capital	19,137	7,263
Total cash (outflow) inflow from operations	(12,912)	20,048
Financing Activities		
Long-term obligations—incurred	231,605	320
—repaid	(9,557)	(22,496)
Interest expense (Note 10)	(81,302)	(68,701)
Dividend paid	(12,000)	—
Net cash inflow (outflow) from financing activities	128,746	(90,877)
Investing Activities		
Additions to—fixed assets—sustaining	2,158	11,203
—fixed assets—plant construction	19,343	47,457
—deferred charges	8,909	4,390
Net cash outflow from investing activities	30,410	63,050
Increase (decrease) in short-term debt	(85,424)	133,879
Short-term debt—beginning of year	160,145	26,266
Short-term debt—end of year	\$ 74,721	\$ 160,145

Notes to Consolidated Financial Statement

Note 1

Significant Accounting Policies

The Corporation's accounting policies are in accordance with generally accepted accounting principles. The following policies are considered to be significant:

Principles of consolidation

The consolidated financial statements include the accounts of the Corporation and the wholly owned subsidiaries:

- Potash Corporation of Saskatchewan Sales Limited (PCS Sales)
 - PCS Sales (Iowa) Inc.
 - PCS Sales (Indiana) Inc.
- Potash Corporation of Saskatchewan Mining Limited (PCS Mining)
- Potash Corporation of Saskatchewan Transport Limited (PCS Transport)

PCS Transport has 64% interest in Canpotex Bulk Terminals Limited which is accounted for by the equity method.

Inventories

Inventories of product and raw ore are valued at the lower of average cost or net realizable value. Cost is determined using the first in, first out (FIFO) method and is based on the monthly average of mine production costs. Inventories of materials and supplies are valued at the lower of average cost or replacement cost.

Fixed Assets

Fixed assets are carried at cost. Cost of additions, betterments and renewals are capitalized.

Maintenance and repair expenditures which do not improve or extend productive life are expensed as incurred. Interest associated with major capital projects is capitalized during the construction period at the Corporation's average cost of long-term debt, and is included in the total cost of the project.

Depreciation and amortization

Depreciation and amortization are provided on a basis and at rates calculated to amortize the cost of the fixed assets over their estimated useful lives, as set out below:

	Depreciation or Amortization Basis	Approximate Rate
Head Office		
Furniture, equipment and leasehold improvements	Straight-line	10%
Automotive equipment	Straight-line	20%
Mines		
All mine assets	Units of production	
Offsite Storage Facilities		
Buildings, roads and sites	Straight-line	4%
Equipment	Straight-line	8%

Research and development costs

Research costs are charged to expense as incurred.

Development costs are capitalized until a project is determined not to be technically or economically feasible and no future benefit to the Corporation exists, at which time the costs are expensed.

Deferred Charges

Issue costs of long-term obligations are amortized over the term of the related liability.

Other development costs which are capitalized are amortized over the estimated useful life of the project to which they relate.

Note 1 (continued)**Foreign exchange translation**

Sales revenues are translated to Canadian dollars at the average exchange rate for each month, or the applicable forward exchange contract rate. Other operating transactions are translated to Canadian dollars at the average exchange rate for each month.

Monetary assets and liabilities are translated at year-end exchange rates.

Non-monetary assets are translated at the exchange rate prevailing at the time of the transaction.

Long-term liabilities are translated on the basis of year-end exchange rates. Unrealized exchange gains and losses relating to this translation are deferred and amortized over the remaining life of the liability.

Leases

Leases entered into are classified as either capital or operating leases. Leases that transfer substantially all of the benefits and risks of ownership of property to the Corporation are accounted for as capital leases. At the time a capital lease is entered into, an asset is recorded together with the related long-term obligation. Equipment acquired under capital leases is being depreciated on the same basis as other fixed assets. Gains or losses resulting from sale-leaseback transactions are deducted from the cost of equipment under capital lease and amortized on the same basis as the related asset. Rental payments under operating leases are charged to expense as incurred.

Note 2**Change in Accounting Policy**

In 1986, the company changed the basis of valuing product inventory from the average cost method to the first-in, first-out method. This change in accounting policy does not have a significant effect on the current year's consolidated financial statements, and has no effect on prior year's consolidated financial statements.

Note 3**Financing Requirements**

The corporation has incurred significant losses in recent years. The Corporation's ability to continue is dependent on the attainment of profitable operations or the provision of additional financing.

Note 4**Inventories**

	(Thousands)	
	1986	1985
Product	\$ 22,202	\$ 28,251
Raw ore	2,138	2,709
Materials and supplies	22,703	20,990
	\$ 47,043	\$ 51,950

Note 5**Fixed Assets**

	(Thousands)	
	1986	1985
Land	\$ 19,633	\$ 19,414
Buildings and improvements	206,583	207,808
Machinery and equipment	555,250	555,912
Plant under construction	406,911	349,281
Deferred exploration and development costs	115,712	111,995
Equipment under capital lease	108,072	108,032
	1,412,161	1,352,442
Less: Accumulated depreciation and amortization	247,417	221,758
	\$ 1,164,744	\$ 1,130,684

Note 6

Deferred Charges and Investment

	(Thousands)	
	1986	1985
Deferred charges—net		
Issue costs—long-term obligations	\$ 7,243	\$ 3,768
System development and other	158	373
Preproduction costs	3,999	2,723
Research studies	4,979	2,372
Esterhazy brine leak costs	4,722	—
	21,102	9,236
Unrealized foreign exchange losses	10,742	22,648
Investment, at equity	31,844	31,884
	965	965
	\$ 32,809	\$ 32,849

Note 7

Long-Term Debt

	(Thousands)	
	1986	1985
Province of Saskatchewan		
■ Matures on March 15, 1989, with interest at 16% per annum, payable annually (US \$75,000)	\$ 103,537	\$ 104,813
■ Matures on August 15, 1992, with interest at 15% per annum, payable annually (US \$50,000)	69,025	69,875
■ Matures on March 15, 1990, with interest at 10.75% per annum, payable annually (US \$50,000)	69,025	69,875
■ Matures on December 21, 1988, with interest at 10.75% per annum, payable semi-annually	80,000	80,000
■ Matures on March 5, 1991, with interest at 8.5% per annum, payable annually (US \$115,000)	158,758	—
■ Matures on July 24, 1991, with interest at 7.5% per annum, payable annually (US \$50,000)	69,025	—
Saskatchewan Heritage Fund		
■ Matures on June 30, 1987, with interest at 9.3% per annum, payable semi-annually	5,000	10,000

Note 7 (continued)

Long-Term Debt (continued)

	(Thousands)	
	1986	1985
Webster County, Iowa		
• Matures December 1, 1996, with interest at 13% per annum payable semi-annually (US \$3,900)	\$ 5,384	\$ 5,450
City of Portage, Indiana		
• Matures in six equal annual installments on March 1, 1987 to 1992 inclusive with interest at 12.25% per annum, payable quarterly secured by assets of PCS Sales (Indiana) Inc. (US \$3,000)	4,142	4,891
	563,896	344,904
Less amounts due within one year	5,690	5,699
	\$ 558,206	\$ 339,205

Principal payments due on long-term debt for the next five years are as follows:

(thousands)	1987 — \$ 5,690	1990 — \$ 69,715
	1988 — \$ 80,690	1991 — \$228,472
	1989 — \$104,227	

Note 8

Lease Commitments

The Corporation has long-term lease agreements, the longest of which expires in 2005. Future minimum lease payments under these capital and operating leases will be approximately as follows:

	(Thousands)	
	Operating	Capital
Years ending December 31		
1987	\$ 10,533	\$ 16,859
1988	7,686	16,859
1989	6,362	16,859
1990	3,716	16,859
1991	2,488	16,859
Subsequent years	15,687	125,864
Less—amount representing interest		210,159
		(102,084)
Present value of minimum capital lease payments		108,075
Current obligation		3,867
Long-term portion		\$ 104,208

Note 9**Province of Saskatchewan Investment**

	(Thousands)	
	1986	1985
Saskatchewan Heritage Fund	\$ 418,554	\$ 418,554
Crown Investments Corporation of Saskatchewan	62,000	62,000
	\$ 480,554	\$ 480,554

Note 10**Interest Expense**

	(Thousands)	
	1986	1985
Interest on		
—Long-term debt	\$ 60,117	\$ 47,422
—Short-term debt	7,612	7,712
—Obligations under capital lease	13,573	13,567
	81,302	68,701
Less capitalized interest	38,218	36,715
	\$ 43,084	\$ 31,986

Note 11**Income Taxes**

By virtue of the fact that the Corporation is wholly owned by the Province of Saskatchewan, neither it nor its wholly owned subsidiaries are subject to Federal or Provincial income taxes in Canada. Certain income and assets of its subsidiaries and affiliates are subject to Federal and State taxes in the United States.

Note 12**Contractual Obligations and Commitments**

The Corporation is expanding its Lanigan Division at estimated cost, including capitalized interest, of \$559,527,000 of which approximately \$557,149,000 has been expended to date.

PCS Sales is a shareholder in Canpotex Limited, an offshore marketing company. Should any operating losses be incurred by Canpotex Limited, they will be proportionately shared by its shareholders. PCS Sales is also a guarantor of the performance by Canpotex Limited for certain railcar leases.

PCS Sales and PCS Mining have guaranteed a mortgage loan not to exceed \$4,300,000 for warehousing facilities in Danville, Illinois.

Note 13**Directors and Officers**

The aggregate 1986 remuneration to directors and senior officers amounted to \$1,066,620 (1985 - \$1,109,000).

Note 14

Related Party Transactions

Included in these consolidated financial statements are expense amounts resulting from routine operating transactions conducted at prevailing market prices with various Saskatchewan Crown controlled departments, agencies and corporations with which the Corporation is related. Account balances resulting from these transactions are included in the Consolidated Statement of Financial Position and are settled on normal trade terms.

Other amounts due to or from related parties and the terms of settlement are described separately in the consolidated financial statements and the notes thereto.

Note 15

Pensions

Substantially all employees of the Corporation are participants in either a defined contribution or a defined benefit based pension plan.

Note 16

Contingency

On February 10, 1987, Lundberg Industries Ltd. and New Mexico Potash Corporation filed a petition with the International Trade Administration, U.S. Department of Commerce, and the United States International Trade Commission for the imposition of antidumping duties against imports of Canadian produced muriate of potash alleged to be the cause of or to threaten material injury to the U.S. industry. The Corporation will participate in the proceeding and will deny the allegations.

Note 17

Comparative Figures

Certain of the prior year's comparative figures have been reclassified to conform with the current year's presentation.

Board of Directors
(at March 31, 1987)

- **Paul J. Schoenhals, Saskatoon**
Chairman of the Board
- **Honourable J. Gary Lane, Q.C.**
Minister of Finance
Province of Saskatchewan
and Minister-in-Charge of PCS
- * **Josie Black, Regina**
Farmer
- * **Al Brissette, Delisle**
Retired
- + **William M. Elliott, Q.C., Regina**
Partner
Law Office, MacPherson,
Leslie & Tyerman
- Donald Flamme, Carievale**
Farmer
- William Gibson, Regina**
President,
Crown Management Board
- * **Peter Golf, Saskatoon**
Peter Golf Enterprises
- + **Dallas Howe, Saskatoon**
President, BDM Systems Ltd.
- * **Brent Logan, Calgary**
President,
Brentwood Ford Sales Ltd.
- Dr. Andy Schmitz, Saskatoon**
Professor,
University of Saskatchewan
- **Earl Silcox, Carlyle**
Farmer/Rancher
- Graham Walker, Regina**
Chairman
Crown Management Board
- + **J. Gordon Wicijowski, F.C.A., Regina**
Managing Partner,
Clarkson Gordon
- * Member of Audit Committee
- + Member of
Compensation Committee
- Member of
Executive Committee

**Potash Corporation
of Saskatchewan
Mining Limited**

- James J. Rubnick**
Executive in Charge
of PCS Mining
- Floyd E. Pellan**
Director,
Group Services
- Graeme Strathdee**
Director,
Research & Development
- Garth Moore**
General Manager,
Rocanville Division
- Rick Lacroix**
General Manager,
Cory Division
- Jim Johnstone**
General Manager,
Allan Division
- Rob McCallum**
General Manager,
Lanigan Division

**Potash Corporation
of Saskatchewan
Sales Limited**

- Douglas E. Logsdaile**
Executive in Charge
of PCS Sales
- Sid S. Blair**
Director of Sales
(Canadian & National
Accounts)
- Jim M. DeLong**
Director of Sales
(Industrial Products &
Product Development)
- Jack O. Ellis**
Director of Sales
(Co-op Accounts &
Inventory Management)
- Barry R. Jarrett**
Director of Sales
U.S. Branch
- William G. Irvine**
Director of
Transportation

Management
(at March 31, 1987)

- Charles E. Childers**
President & Chief
Executive Officer
- Keith E. Barton**
Vice President,
General Counsel
and Secretary
- Peter Braun**
Director of
Internal Audit
- Barry Humphreys**
Controller

**The Head Offices for
the Potash Corporation
of Saskatchewan,
PCS Sales and PCS
Mining are located at:**

PCS Tower

Suite 500
122 - 1st Avenue South
Saskatoon, Saskatchewan
S7K 7G3
Phone: (306) 933-8500
Wats: (800) 667-3930
Telex: 074-2699
Telecopier: (306) 652-2699

**PCS Sales
Chicago Office:**

Suite 120
3030 Salt Creek Lane
Arlington Heights, Illinois
60005
Phone: (312) 392-2200
Wats: (800) 241-6908
TWX: (910) 221-2912
Telex: 392-3107
Telecopier: (312) 392-2598

**PCS Mining
Divisions:**

Cery Division

P.O. Box 1320
Saskatoon, Saskatchewan
S7K 2N8
Phone: (306) 382-0525
Telex: 074-2682

Rocanville Division

Rocanville, Saskatchewan
S0A 3L0
Phone: (306) 645-2870
Telex: 971-2342

Esterhazy Division

P.O. Box 1060
Esterhazy, Saskatchewan
S0A 0X0
Phone: (306) 745-6601
Telex: 075-87856

Lanigan Division

P.O. Box 3100
Lanigan, Saskatchewan
S0K 2M0
Phone: (306) 365-2030
Telex: 074-2318

Allan Division

Allan, Saskatchewan
S0K 0C0
Phone: (306) 257-3312
Telex: 074-2634